

ORIGINAL

OPEN MEETING



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MEMORANDUM

Arizona Corporation Commission

DOCKETED

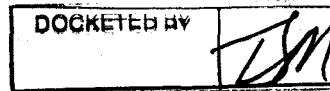
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TO: THE COMMISSION

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2012 DEC 24 P 1:01

FROM: Utilities Division



AZ CORP COMMISSION
DOCKET CONTROL

DATE: December 24, 2012

RE: IN THE MATTER OF THE APPLICATION OF XO COMMUNICATIONS SERVICES, INC. AND ITS AFFILIATES FOR A LIMITED WAIVER OF THE RULES GOVERNING PUBLIC UTILITY HOLDING COMPANIES AND AFFILIATED INTERESTS. (DOCKET NO. T-04302A-12-0456)

Introduction

On November 6, 2012, XO Holdings ("XO Holdings"), XO Communications, LLC ("XO LLC") and XO Communications Services, Inc. ("XOCS") filed an application with the Arizona Corporation Commission ("Commission") for a limited waiver of A.A.C. R14-2-801, *et seq.* (the "Rules") – the rules governing public utility holding companies and affiliated interests. The limited waiver will be used in future transactions which meet the definition of a reorganization under Rule 14-2-801(5) and to consummate transactions otherwise subject to A.A.C. R14-2-804(B). XOCS is not requesting a waiver of A.A.C. R14-2-805 - Annual Filing Requirements of Diversification Activities and Plans.

Background

XOCS is authorized by the Commission to provide competitive local exchange services (including switched and dedicated access services), intraLATA toll services and intrastate interexchange telecommunications services within the State of Arizona.

XO LLC is the parent company to XOCS and a number of similar subsidiaries. XO LLC is a provider of local and long distance telecommunications to businesses, large enterprises and telecommunications carriers and is a direct wholly owned subsidiary of XO Holdings, a Delaware general partnership.

Under the Rules, Commission approval is required per A.A.C. R14-2-803(A) whenever a utility or an affiliate intends to reorganize an existing public utility holding company. Prior approval is also required under R14-2-804(B) if a public utility wishes to "obtain a financial interest in any affiliate not regulated by the Commission, or guarantee, or assume the liabilities of such affiliate" or lend to any affiliate not regulated by the Commission \$100,000 or more for over one year. When companies such as XO LLC or XO Holdings, with entities controlling assets and network facilities spread across the nation, add or replace an investor or participate in any sort of merger, financing, refinancing, reconfiguration, or consolidation, the Rules require Arizona Commission approval.

The Applicant's Request for Waiver of the Rules

The Applicant represents the following in its application:

Given today's market conditions, and the opportunity for new funding and refinancing for competitive telecommunications networks, it is very likely XO Holdings and XO LLC will be parties to future transactions that would be considered "Reorganizations," as that term is broadly defined by the Rules. Additionally, XO LLC and XO Holdings will continue to adjust the assets and debts of all of their subsidiaries and affiliates to maximize network quality, reach and efficiency. Financing and refinancing growth is an integral part of forward-looking strategic planning. A waiver of R14-2-803 and R13-2-804(B) will permit XO LLC and XO Holdings to enter into certain transactions without first seeking ACC approval. XOCS seeks a waiver that would be applicable to it (XOCS) and all of its current and future affiliated entities.

XOCS is a national telecommunications provider with only a fraction of its revenues and investments in Arizona. In the coming years, XOCS will enter into transactions all over the United States that have no impact on Arizona operations. These transactions - reorganizations under the rules - will not result in any fundamental change in the affiliate entity that operates in Arizona and should not be subject to a Commission approval requirement.

XOCS is a non-dominant carrier and, as such, does not exercise monopoly power over a captive service territory or guaranteed revenue base. The Rules were promulgated to protect captive utility ratepayers from rates that "include costs associated with holding company structure, financially beleaguered affiliates, or sweetheart deals with affiliates."¹

XOCS participates in a telecommunications services industry that is energized by market forces such as consumer demand, competitive pricing and the drive to increase market share through added value and technological innovation. Given that XOCS faces competition in all of the retail services it provides to Arizona customers, there exists virtually no incentive or opportunity for XOCS to attempt to extract from customers unduly high or above-market prices that could be used to subsidize unregulated, affiliated interests. The market effectively provides a natural safeguard against the improper exploitation of telecommunication service profits by XOCS.

Approval of a limited waiver will allow the market to realize the benefits of future reorganizations without a separate application to this Commission for each reorganization subject to the Rules. If every certified carrier in Arizona (and each national and international affiliate thereof) sought Commission approval before acquiring new debt, accepting new investment, or purchasing additional assets, the Commission Staff would be inundated by reorganization approval applications. Most of these transactions do not impact Arizona consumers and should not occupy scarce Commission resources. The Rules should be waived by

¹ T-04302A-12-0456, In the matter of the application of XO Communications Services, Inc. and its' affiliates for a limited waiver of the rules governing public utility holding companies and affiliated interests, page 6.

the Commission for entities such as XOCS which: (1) operate nationally with many affiliates; (2) compete in end-user retail markets with alternative service providers; (3) have no guaranteed source of revenue; and (4) are subject to strong competitive pressures to keep prices low and service quality high.

Staff's Analysis and Conclusions

The Application cites seven examples of Commission decisions granting limited waivers for XOCS' competitors in Arizona.² Three decisions pertaining to Competitive Local Exchange Carriers ("CLECs") were issued during a brief timeframe (May 17, 2000 – June 30, 2000) and include similar Staff reasoning in support of a limited waiver - "Staff believes that actions taken by both federal and state regulatory bodies, including this Commission, are increasing competition in the telecommunications industry, including basic local service." Most recently, the Commission stated similar reasoning in Decision No. 73245, dated June 26, 2012, to grant a comparable waiver to tw telecom. "...In this regulatory climate, Staff also believes that the Rules may be unnecessarily restrictive and expensive and that the market may replace the historical need for the Rules for some companies."³

The Application requests limited waivers of the Rules similar to those granted in Decision Nos. 58258, for AT&T Communications of the Mountain States, Inc., and 60728, for Teleport Communications Group and AT&T Corporation. Such waivers would waive the requirements of R14-2-804 and require XOCS to file a notice of intent only for those organizations or reorganizations that are likely to have a material adverse impact on XOCS's Arizona public utilities.

Staff notes, however, that in each of the four most recent waivers the companies are "required to file a notice of intent to enter into the transactions listed in A.A.C. R14-2-803 when a transaction is likely to result in 1) significant increased capital costs of the Arizona operations; 2) significant additional costs allocated or charged directly to the Arizona jurisdiction; or 3) a significant reduction of net income to the Arizona operations."⁴ All four decisions also granted a limited waiver of A.A.C. R14-2-804 while ordering that companies "seek Commission approval for transactions that are likely to have a material adverse effect on Arizona operations."

Staff research disclosed that the requests for limited waivers in past applications were not based on companies experiencing large numbers of past transactions but the expectations that many future transactions would arise from growing multi-state operations. Previous to Cox

² Qwest Corporation/CenturyLink, Decision No. 64654, March 25, 2002, reaffirmed in Decision No. 72493, July 25, 2011; AT&T Communications of the Mountain States, Inc., Decision No. 58258, April 8, 1993; Teleport Communications Group and AT&T Corporation, Decision No. 60728, March 23, 1998; American Communications Services of Pima County, Inc., Decision No. 62616, June 9, 2000; MCI Communications Services, Inc., Decision No. 62702, June 30, 2000; Cox Arizona Telcom L.L.C., Decision No. 62582, May 17, 2000.

³ T-03943A-11-0462, In the matter of the application of tw telecom of arizona llc and tw telecom inc. and their affiliates for a limited waiver of the rules governing public utility holding companies and affiliated rules

⁴ American Communications Services of Pima County, Inc., Decision No. 62616, June 9, 2000; MCI Communications Services, Inc., Decision No. 62702, June 30, 2000; Cox Arizona Telcom L.L.C., Decision No. 62582, May 17, 2000; tw telecom of Arizona llc, Decision No. 73245

THE COMMISSION

December 24, 2012

Page 4

Arizona Telcom, L.L.C. ("Cox") receiving its limited waiver in Decision 62582 on May 17, 2000, Cox had only filed one application for approval of a transaction that was subject to the Rules.⁵ Previous to MCI Communications Services, Inc. ("MCI") receiving its limited waiver in Decision 62702 on June 30, 2000, MCI had made no filings to request Commission approval of any transactions that were subject to the Rules. Previous to American Communications Services of Pima County, Inc. ("ACSI") receiving its limited waiver in Decision 62616 on June 9, 2000, ACSI had not filed any transactions to which the Rules would apply.


Staff is not aware of any evidence that would call into question past Commission decisions that granted limited waivers of the Rules. No complaints have been filed against any party with a limited waiver of the Rules alleging conduct that could have been prevented by the Commission's denial of limited waivers of the Rules. None of the companies receiving limited waivers of the Rules have filed any indications that the Rules, as waived, remain burdensome.

Recommendations

Staff recommends that the application filed by XO Holdings, XO LLC and XOCS for a limited waiver of the Rules be approved subject to the condition that the companies be required to file a notice of intent to enter into the transactions listed in A.A.C. R14-2-803 when a transaction is likely to result in:

1. significant increased capital costs of the Arizona operations;
2. significant additional costs allocated or charged directly to the Arizona jurisdiction; or
3. a significant reduction of net income to the Arizona operations.

Staff also recommends that XO Holdings, XO LLC and XOCS be granted a limited waiver of A.A.C. R14-2-804 on the condition that they seek Commission approval for transactions that are likely to have a material effect on Arizona operations.

for 
Steven M. Olea, Director
Utilities Division

SMO:AFF:sms\BH

ORIGINATOR: Armando F. Fimbres

⁵ T-03471A-99-0488, Joint application of Cable Plus Company, L.P., d/b/a Telephone Plus, and Cox Arizona Telecom, L.L.C. for an order approving the sale and transfer of assets of Telephone Plus, Decision No. 61970, October 1, 1999.

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BEFORE THE ARIZONA CORPORATION COMMISSION

GARY PIERCE
Chairman
BOB STUMP
Commissioner
SANDRA D. KENNEDY
Commissioner
PAUL NEWMAN
Commissioner
BRENDA BURNS
Commissioner

IN THE MATTER OF THE APPLICATION
OF XO COMMUNICATIONS SERVICES,
INC. AND ITS AFFILIATES FOR A
LIMITED WAIVER OF THE RULES
GOVERNING PUBLIC UTILITY HOLDING
COMPANIES AND AFFILIATED
INTERESTS.

DOCKET NOS. T-04302A-12-0456

DECISION NO. _____
ORDER

Open Meeting
January 30 and January 31, 2013
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. On November 6, 2012, XO Holdings ("XO Holdings"), XO Communications, LLC ("XO LLC") and XO Communications Services, Inc. ("XOCS") filed an application with the Arizona Corporation Commission ("Commission") for a limited waiver of A.A.C. R14-2-801, et seq. (the "Rules") – the rules governing public utility holding companies and affiliated interests.
2. The limited waiver will be used in future transactions which meet the definition of a reorganization under Rule 14-2-801(5) and to consummate transactions otherwise subject to A.A.C. R14-2-804(B).
3. XOCS is not requesting a waiver of A.A.C. R14-2-805 - Annual Filing Requirements of Diversification Activities and Plans.

1 Background

2 4. XOCS is authorized by the Commission to provide competitive local exchange
3 services (including switched and dedicated access services), intraLATA toll services and
4 intrastate interexchange telecommunications services within the State of Arizona.

5 5. XO LLC is the parent company to XOCS and a number of similar subsidiaries.
6 XO LLC is a provider of local and long distance telecommunications to businesses, large
7 enterprises and telecommunications carriers and is a direct wholly owned subsidiary of XO
8 Holdings, a Delaware general partnership.

9 6. Under the Rules, Commission approval is required per A.A.C. R14-2-803(A)
10 whenever a utility or an affiliate intends to reorganize an existing public utility holding
11 company.

12 7. Prior approval is also required under R14-2-804(B) if a public utility wishes to
13 "obtain a financial interest in any affiliate not regulated by the Commission, or guarantee, or
14 assume the liabilities of such affiliate" or lend to any affiliate not regulated by the Commission
\$100,000 or more for over one year.

15 8. When companies such as XO LLC or XO Holdings, with entities controlling
16 assets and network facilities spread across the nation, add or replace an investor or participate
17 in any sort of merger, financing, refinancing, reconfiguration, or consolidation, the Rules
18 require Arizona Commission approval.

19 The Applicant's Request for Waiver of the Rules

20 The Applicant represents the following in its Application:

21 9. Given today's market conditions, and the opportunity for new funding and
22 refinancing for competitive telecommunications networks, it is very likely XO Holdings and
23 XO LLC will be parties to future transactions that would be considered "Reorganizations," as
24 that term is broadly defined by the Rules.

25 10. Additionally, XO LLC and XO Holdings will continue to adjust the assets and
26 debts of all of their subsidiaries and affiliates to maximize network quality, reach and
27 efficiency. Financing and refinancing growth is an integral part of forward-looking strategic
28 planning. A waiver of R14-2-803 and R13-2-804(B) will permit XO LLC and XO Holdings to

1 enter into certain transactions without first seeking ACC approval. XOCS seeks a waiver that
2 would be applicable to it (XOCS) and all of its current and future affiliated entities.

3 11. XOCS is a national telecommunications provider with only a fraction of its
4 revenues and investments in Arizona. In the coming years, XOCS will enter into transactions
5 all over the United States that have no impact on Arizona operations. These transactions -
6 reorganizations under the rules - will not result in any fundamental change in the affiliate
7 entity that operates in Arizona and should not be subject to a Commission approval
8 requirement.

9 12. XOCS is a non-dominant carrier and, as such, does not exercise monopoly
10 power over a captive service territory or guaranteed revenue base. The Rules were
11 promulgated to protect captive utility ratepayers from rates that "include costs associated with
12 holding company structure, financially beleaguered affiliates, or sweetheart deals with
13 affiliates."¹

14 13. XOCS participates in a telecommunications services industry that is energized
15 by market forces such as consumer demand, competitive pricing and the drive to increase
16 market share through added value and technological innovation. Given that XOCS faces
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18 no incentive or opportunity for XOCS to attempt to extract from customers unduly high or
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20 market effectively provides a natural safeguard against the improper exploitation of
21 telecommunication service profits by XOCS.

22 14. Approval of a limited waiver will allow the market to realize the benefits of
23 future reorganizations without a separate application to this Commission for each
24 reorganization subject to the Rules. If every certified carrier in Arizona (and each national and
25 international affiliate thereof) sought Commission approval before acquiring new debt,
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2 Arizona consumers and should not occupy scarce Commission resources. The Rules should be
3 waived by the Commission for entities such as XOCS which: (1) operate nationally with many
4 affiliates; (2) compete in end-user retail markets with alternative service providers; (3) have no
5 guaranteed source of revenue; and (4) are subject to strong competitive pressures to keep
6 prices low and service quality high.

7 Staff's Analysis and Conclusions

8 15. The Application cites seven examples of Commission decisions granting limited
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14 Most recently, the Commission stated similar reasoning in Decision No. 73245, dated June 26,
15 2012, to grant a comparable waiver to tw telecom.³ "...In this regulatory climate, Staff also
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20 Teleport Communications Group and AT&T Corporation. Such waivers would waive the
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22 organizations or reorganizations that are likely to have a material adverse impact on XOCS's
23 Arizona public utilities.

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25 2011; AT&T Communications of the Mountain States, Inc., Decision No. 58258, April 8, 1993; Teleport
26 Communications Group and AT&T Corporation, Decision No. 60728, March 23, 1998; American Communications
27 Services of Pima County, Inc., Decision No. 62616, June 9, 2000; MCI Communications Services, Inc., Decision No.
28 62702, June 30, 2000; Cox Arizona Telcom L.L.C., Decision No. 62582, May 17, 2000.

³ T-03943A-11-0462, In the matter of the application of tw telecom of arizona llc and tw telecom inc. and their
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⁴ T-03943A-11-0462, In the matter of the application of tw telecom of arizona llc and tw telecom inc. and their
affiliates for a limited waiver of the rules governing public utility holding companies and affiliated rules

1 17. Staff notes, however, that in each of the four most recent waivers⁵ the
2 companies are "required to file a notice of intent to enter into the transactions listed in A.A.C.
3 R14-2-803 when a transaction is likely to result in (1) significant increased capital costs of the
4 Arizona operations; (2) significant additional costs allocated or charged directly to the Arizona
5 jurisdiction; or (3) a significant reduction of net income to the Arizona operations." All four
6 decisions also granted a limited waiver of A.A.C. R14-2-804 while ordering that companies
7 "seek Commission approval for transactions that are likely to have a material adverse effect on
8 Arizona operations."

9 18. Staff research disclosed that the requests for limited waivers in past applications
10 were not based on companies experiencing large numbers of past transactions but the
11 expectations that many future transactions would arise from growing multi-state operations.
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17 Communications Services of Pima County, Inc. ("ACSI") receiving its limited waiver in
18 Decision 62616 on June 9, 2000, ACSI had not filed any transactions to which the Rules
19 would apply.

20 19. Staff is not aware of any evidence that would call into question past
21 Commission decisions that granted limited waivers of the Rules. No complaints have been
22 filed against any party with a limited waiver of the Rules alleging conduct that could have
23 been prevented by the Commission's denial of limited waivers of the Rules. None of the
24 companies receiving limited waivers of the Rules have filed any indications that the Rules, as
25 waived, remain burdensome.

26 ...

27 _____
28 ⁵ American Communications Services of Pima County, Inc., Decision No. 62616, June 9, 2000; MCI Communications Services, Inc., Decision No. 62702, June 30, 2000; Cox Arizona Telcom L.L.C., Decision No. 62582, May 17, 2000.

20. Staff recommends that the application filed by XO Holdings, XO LLC and XOCs for a limited waiver of the Rules be approved subject to the condition that the companies be required to file a notice of intent to enter into the transactions listed in A.A.C. R14-2-803 when a transaction is likely to result in:

- A. significant increased capital costs of the Arizona operations;
- B. significant additional costs allocated or charged directly to the Arizona jurisdiction; or
- C. a significant reduction of net income to the Arizona operations.

21. Staff also recommends that XO Holdings, XO LLC and XOCS be granted a limited waiver of A.A.C. R14-2-804 on the condition that they seek Commission approval for transactions that are likely to have a material effect on Arizona operations.

CONCLUSIONS OF LAW

1. XO Communications Services, Inc. is a public service corporation within the meaning of Article XV of the Arizona Constitution.

2. The Commission has jurisdiction over XO Communications Services, Inc. and the subject matter in this filing.

3. The Commission, having reviewed the filing and Staff's Memorandum dated December 11, 2013, concludes that it is in the public interest to grant approval as proposed and discussed herein.

ORDER

IT IS THEREFORE ORDERED that the application of XO Holdings, XO Communications, LLC and XO Communications Services, Inc. seeking a limited waiver of A.A.C. R14-2-803 and R14-2-804 be and hereby is approved.

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1 IT IS FURTHER ORDERED that XO Holdings, XO Communications, LLC and XO
2 Communications Services, Inc. are required to file a notice of intent to enter into the transactions
3 listed in A.A.C. R14-2-803 when a transaction is likely to result in – (1) significant increased
4 capital costs of the Arizona operations; (2) significant additional costs allocated or charged directly
5 to the Arizona jurisdiction; or (3) a significant reduction of net income to the Arizona operations.

6 IT IS FURTHER ORDERED that that XO Holdings, XO Communications, LLC and XO
7 Communications Services, Inc. be and hereby are granted a limited wavier of A.A.C. R14-2-804
8 on the condition that they seek Commission approval for transactions that are likely to have a
9 material effect on Arizona operations.

10 IT IS FURTHER ORDERED that this Decision shall be become effective immediately.

11 **BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

12
13 _____
CHAIRMAN

COMMISSIONER

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COMMISSIONER

COMMISSIONER

COMMISSIONER

17
18 IN WITNESS WHEREOF, I, ERNEST G. JOHNSON,
19 Executive Director of the Arizona Corporation Commission,
20 have hereunto, set my hand and caused the official seal of
this Commission to be affixed at the Capitol, in the City of
Phoenix, this _____ day of _____, 2013.

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23 _____
ERNEST G. JOHNSON
24 EXECUTIVE DIRECTOR

25 DISSENT: _____

26
27 DISSENT: _____

28 SMO:AFF:sms/BH

Decision No. _____

1 SERVICE LIST FOR: XO Communications Services, Inc.
2 DOCKET NO. T-04302A-12-0456

3 Joan Burke
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5 1650 North First Avenue
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